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No. 88-516

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

LIBERTY NATIONAL BANK AND TRUST COMPANY,
Petitioner,

v.

STATE OF NORTH DAKOTA,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NORTH DAKOTA

BRIEF OF THE AMERICAN BANKERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF THE PETITION

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QUESTION PRESENTED FOR REVIEW

Whether the court below correctly decided that the National Bank Act, which establishes the allowable period for national banks to hold real estate acquired in satisfaction of debts previously contracted, does not preempt provisions of the North Dakota corporate farming law, which establishes a shorter holding period for national banks in North Dakota with respect to ranchland and farmland acquired in satisfaction of debts previously contracted.

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MISCELLANEOUS:

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INTEREST OF THE AMICUS CURIAE

In this case, the Supreme Court of North Dakota held that the state's three-year maximum period for a "corporation" to hold farmland was applicable to the Petitioner, a national bank. This decision was made notwithstanding the fact that federal law authorizes the Petitioner to hold real estate for up to five years. As such, the decision represents a significant assault on the dual federal-state banking system.

In addition to its considerable independent importance, this case is important as a precedent for future state attempts to preempt federal statutes and regulations.

The American Bankers Association has long supported the dual banking system. The system reflects the philosophy and form of United States constitutional government, with its division of powers between the states and the federal government. The checks and balances of the system have contributed significantly to the vitality and progress of commercial banking, and have served as a deterrent to inappropriate or unduly burdensome actions at either the state or national level.

The American Bankers Association is the principal trade association of the commercial banking industry in the United States. There are member banks of the American Bankers Association located in each of the fifty states and the District of Columbia, including banks chartered by the Comptroller of the Currency (National Banks) and banks chartered by the states in which they are located (State Banks).

Almost four thousand commercial banks, primarily small ones, are classified as "agricultural banks," i.e., those with a minimum of twenty-five percent of their lending dedicated to the financing of farms or ranches.[1] In recent years, agricultural banking has experienced extreme difficulties. First, a period of rapid inflation in the value of farmland encouraged farmers to borrow (and banks to lend) in order to purchase additional acreage. This period of inflation,

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[1] Federal Deposit Insurance Corporation, Farm Bank Problems and Related Policy Options at 8-9 (1986).

ending in 1981, was swiftly followed by an equally rapid decline in the value of farmland. From 1982 to 1987 the average value of farmland in the United States declined by thirty-three percent. In North Dakota, the figure was thirty percent between 1981 and 1986. It was within this period of decline that Petitioner would have had to sell the property in question if North Dakota law applied.

From 1987 to 1988, average farmland values increased by seven percent in the region which includes North Dakota.[2] Petitioner's actual sale of the relevant property took place during this period of rising values, as allowed by federal law. The net effect of the fluctuations was that many farm borrowers were, for a period of time, unable to pay their debts to lenders, and the lenders found themselves without adequate security for the loans.[3] Not only did farms themselves fail, but so too did banks which financed them. Of the 138 commercial banks which failed in the United States in 1986, 59 were agricultural banks.[4] In 1987, that situation improved slightly so that 55 agricultural banks failed out of a total of 184.[5]

When a farmer or rancher is unable to repay a loan, often a bank's only recourse is to take title to

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[2] Compare: United States Department of Agriculture, *Agricultural Income and Finance: Situation and Outlook Report* at 18-19 (May 1988) and United States Department of Agriculture, *Farm Sector Financial Problems: Another Perspective* at 8-9 (May 1986) (attached hereto as Exhibits I and II).

[3] Federal Deposit Insurance Corporation, *supra* Note 1, at 24.

[4] *FDIC Insured Banks That Have Failed Or Been Rescued in 1986*, Am. Banker, Jan. 6, 1987, at 14 col. 1.

[5] *1987 Closings Fall Just Below Grim Forecast*, Am. Banker, Jan. 5, 1988 at 1, 3 col. 4.

property by foreclosure or in lieu of foreclosure, and then attempt to sell the property in order to make itself whole. Obviously, it is in the interests not only of the bank, but of the farmer or rancher as well, that the bank receives the best price for the land. In a depressed economy, however, the market value of agricultural property too often does not even approximate the balance of the outstanding loan. Compelling the sale of property at prices which are depressed to begin with, and often in competition with too many other simultaneous distress sales (which tends further to decrease prices) benefits no one. It makes far more sense to permit lenders to hold the land until the market recovers, and that is the sensible choice that Congress made for national banks—most recently in 1980 and 1982.

If a state chooses to force its own state-chartered financial institutions to conduct "fire sales" of property taken in foreclosure, we consider it unfortunate, but acknowledge that it is the state's right to do so. It is not the state's right, however, to impose the same rules upon financial institutions chartered by the United States. It is to represent the interests of those institutions that the ABA respectfully submits this brief as amicus curiae.

ARGUMENT

I.

Whether States May Impose A Shorter Limit On The Time A National Bank May Own Real Estate Than The Period Established By Federal Statute Raises A Substantial Question Of Federal Law Which Should Be Decided By This Court.

This Court has long recognized that state laws may be preempted by federal statutes, *Pacific Gas and Electric v. Energy Resources Commission*, 461 U.S. 190 (1983). This federal preemption may result from explicit preemptive language or it may be implied. In *Pacific Gas and Electric*, this Court set forth that Congress' intent to preempt state law may be implied if there is a:

> 'scheme of federal regulation . . . so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it,' because the Act 'of Congress may touch a field in which the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject,' or because 'the object sought to be obtained by the federal law and the character of obligations imposed by it may reveal the same purpose.'

461 U.S. at 204 (citations omitted).

This Court categorized the circumstances in which federal preemption will be found:

> [S]tate law can be preempted in either of two general ways. If Congress evidences an intent to occupy a given field, any state law falling within that field is preempted . . . . If Congress has not

> entirely displaced state regulation over the matter in question, state law is still preempted to the extent it actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law.

Silkwood v. Kerr-McGee Corp., 464 U.S. 238, 248 (1984) (citations omitted).

Preemption in this case may most obviously be found on the basis of actual conflict. Title 12 U.S.C. Section 29 permits Petitioner to hold the real estate in question for five years while Section 10-06-13 of the North Dakota Century Code purports to limit Petitioner to holding the same real estate for three years. As discussed by the court below, the purpose of allowing a national bank to hold such real estate is to avoid "the adverse consequences of forced divestitures on the banks." *State of North Dakota v. Liberty National Bank*, 427 N.W. 2d 307, 311 (1988). As Congress found a *five* year period to be necessary to protect the safety and soundness of national banks from losses due to "fire sales" of repossessed real estate, then any state law which forces national banks to sell this real estate earlier than allowed by Congress "stands as an obstacle to the accomplishment of the *full* purposes and objectives of Congress." *Silkwood*, 464 U.S. at 248 (emphasis added).

In addition to the actual conflict between the North Dakota and federal statutes, the state statute is preempted because "the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject." *Pacific Gas and Electric*, 461 U.S. at 204. The federal legislative history recited by the North Dakota Supreme Court demonstrates that the federal interest

in regulating ownership of real estate occupies this area of the law to such an extent that the state statute involved is preempted.

II.

Review Of The Decision Of The North Dakota Supreme Court Is Necessary To Resolve An Unsettled Issue of Federal Law.

As noted above, this case involves the ability of a state to override the provisions of 12 U.S.C. Section 29 which limit how long a national bank may hold real property acquired in lieu of foreclosing on a delinquent mortgage. The North Dakota statute allows Petitioner, a national bank, to hold the real estate in question for only three years while Federal law permits Petitioner to hold the same property for five years. N.D. Cent. Code § 10-06-13; 12 U.S.C. § 29. While the property involved in this case has been sold by Petitioner, the holding by the court below still involves a "live" issue because the underlying dispute in this case is "capable of repetition, yet evading review." *Murphy v. Hunt*, 455 U.S. 486 (1982). The period of time in which a case presenting this issue can arise is the two years between the end of the North Dakota statute's three-year maximum holding period and the National Bank Act's five-year limit. A two year period is not normally sufficient for such a case to work its way up to this Court for resolution. For example, even in this relatively speedy case, where the trial court granted a summary judgment and there was no intermediate state appellate court involved, the federal five-year limit passed on September 19, 1988, even before the petition for writ of certiorari was due in this Court. If certiorari is not

granted because the farm involved was sold after the action was commenced, but within the federal five-year limit, then it is unlikely that this issue could ever be reviewed, even though the issue is likely to arise repeatedly in the future. In addition to North Dakota, there are at least two other states with statutes which have limitations on banks holding real estate which are less than that set out at 12 U.S.C. Section 29. *See* N.C. Gen. Stat. § 53-43(3)(c) (1 year); 7 Pa. Cons. Stat. § 202 (2 years).

National banks in these states, as well as North Dakota, will be faced with the same conflict between state and federal statutes. This clearly gives rise to an important question of federal preemption of the state statutes. The overriding issue of federalism involved in this case goes to the very core of the dual banking system and since no federal court has spoken on this precise issue, this Court should settle the question authoritatively by granting certiorari and issuing an opinion in this case.

III.

The Case Was Decided Incorrectly By The Supreme Court Of North Dakota.

Even though it has correctly identified the issue in this case, federal preemption, and cited several of this Court's decisions in the area, the court below has simply erred in applying the relevant law to the facts of this case. The North Dakota court's most obvious error was in finding that there is no "actual conflict" between 12 U.S.C. Section 29 and N.D. Cent. Code Section 10-06-13. The federal statute allows a national bank to hold the property in question for five years while the North Dakota statute limits the same na-

tional bank's ownership of the same property to three years. This is a conflict, pure and simple, unless three years equals five years.

The North Dakota court's long and learned discussion of the two statutes and their legislative histories is, for the most part, irrelevant to the issue of actual conflict. The discourse on this issue by the court below appeared to be an effort to reason that, since the United States Congress and the North Dakota Legislature had similar goals and objectives, the two statutes do not conflict. 427 N.W. 2d at 310-14. It is neither the intentions of the state legislature nor the public policies involved which determine if there is a conflict, it is the substance of the statute involved and the "purposes and objectives of Congress." 427 N.W. 2d at 314. As the court below recognized, the state statute may not stand as an obstacle to the execution of Congressional intent.

The North Dakota court recognized that one of the objectives of Congress was to "provide a measure of protection to banks" 427 N.W. 2d at 315, by allowing them to hold foreclosed real property for long enough to increase the chances that it could be sold at a price "reflecting the bank's investment" 125 Cong. Rec. 14,599 (1979) (Letter from John G. Heimann, Comptroller of the Currency, to William Proxmire, Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate, dated May 31, 1979). The court clearly erred, however, by denominating this objective of Congress as "secondary." One has only to look at the elaborate scheme of banking statutes enacted over the years by Congress to determine that the safety and soundness of banks are of paramount importance. That is why, for example, there is federal

deposit insurance protecting deposits in all FDIC-insured banks. *See Gunter v. Hutcheson*, 674 F.2d 862, 870 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982). That is why federal banking regulatory agencies have been given the authority to take administrative action, including the issuance of cease and desist orders and the suspension and removal of bank directors, officers and employees in the event that a bank is engaging in "an unsafe or unsound practice." 12 U.S.C. §§1818(b), (e), (g) (1980, 1985 Supp.). *See also* S. Rep. No. 1482, 89th Cong., 2d Sess. (1966), *reprinted in* 1966 U.S. Code Cong. & Ad. News 3532-3533. That is why the various federal banking regulatory agencies have been granted the power to conduct periodic examinations of virtually all of the activities of commercial banks. 12 U.S.C. §§ 325, 338, 481, 1820 (1980, 1985 Supp.). That is why there are prohibitions against use of bank deposits for risky or speculative operations. H.R. Rep. 150, 73d Cong., 1st Sess. (May 19, 1933).

As recognized by the court below, national banks "are instrumentalities of the federal government, and are necessarily subject to the paramount authority of the United States." 427 N.W. 2d at 309 (citing *First National Bank v. Missouri*, 263 U.S. 640, 656 (1924)). If North Dakota can override federal statutes and place limits on ownership of real estate by these federal instrumentalities, then it can regulate the ownership of real estate by other federal instrumentalities in contravention of federal statutes. Even the Supreme Court of North Dakota has not suggested that North Dakota can exercise such control over the Federal Deposit Insurance Corporation or the Postal

Service which, like a national bank, are chartered by the authority of the United States.

In summary, 12 U.S.C. Section 29 establishes the period for which a national bank may hold real estate and preempts the shorter period prescribed by the North Dakota statute. This preemption arises from the actual conflict between the state and federal statutes and the dominant federal interest in this area which precludes enforcement of the state statute covering the same subject. The decision of the North Dakota Supreme Court is at variance with the rulings of this Court. It should not be permitted to stand unreviewed and unreversed.

CONCLUSION

For all the reasons stated herein, the American Bankers Association, as amicus curiae, respectfully urges the Court to grant the petition for writ of certiorari.

Respectfully submitted,

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EXHIBITS

EXHIBIT I

United States Department of Agriculture

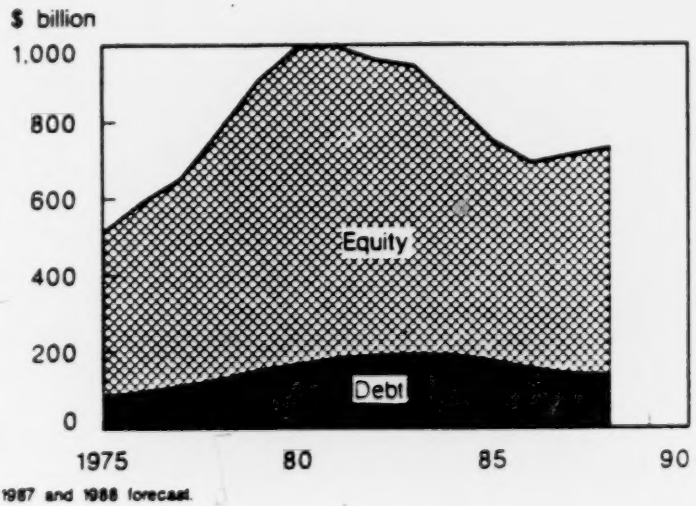
Economic Research Service

AFO-29
May 1988

Agricultural Income and Finance

Situation and Outlook Report

Farm Equity Up Again in 1988



1987 and 1988 forecast.

Figure 9

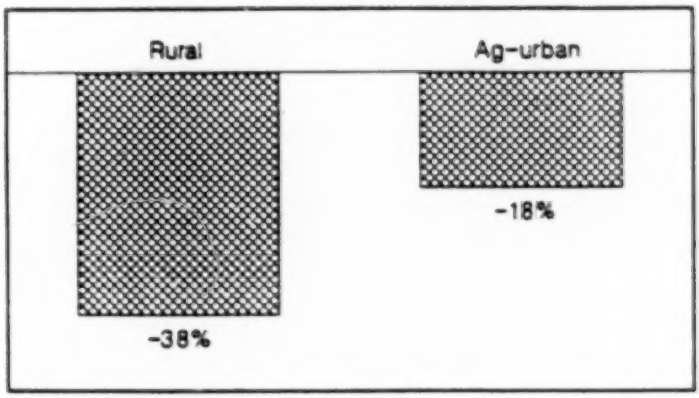
Percent Change in Farmland Value Per Acre, February 1987-88, By Farm Production Regions



[18]

Figure 10

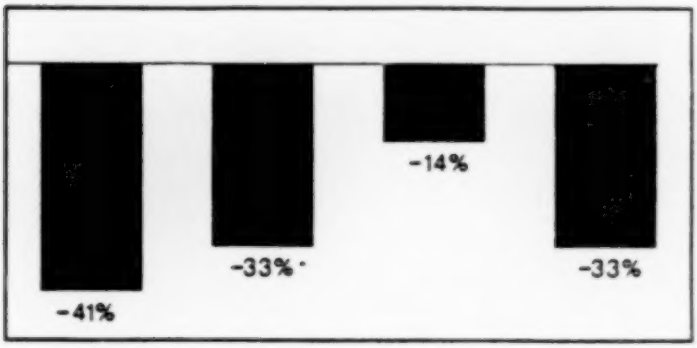
Percent Change in Farmland Value in Ag-Urban and Rural Counties, 1982-87



Excludes Alaska and Hawaii
Source USDA Survey of ASCS County Executive Directors

[19]

Figure 11
Percent Change in Farmland Value by Type, 1982-87



Excludes Alaska and Hawaii
Source: USDA Survey of ASCS County Executive Directors

Figure 12
Change Between Peak in Regional Farmland Value and 1987 Value

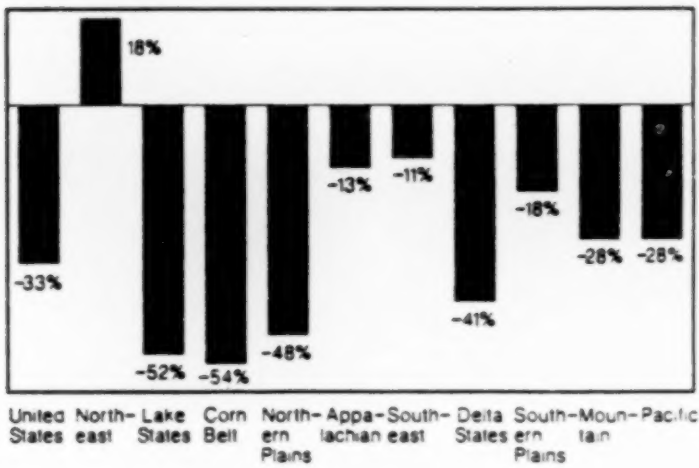


EXHIBIT II

United States
Department of
Agriculture

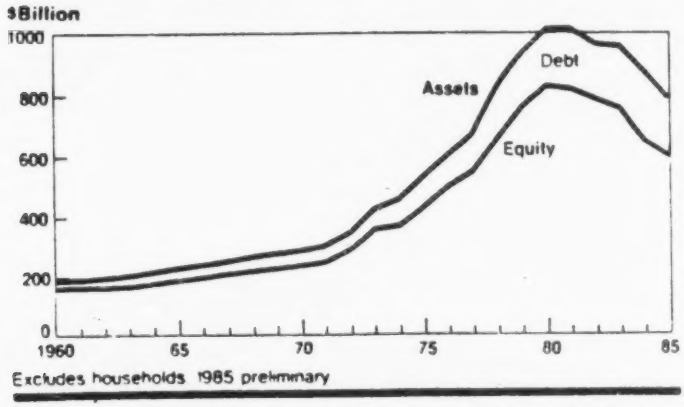
Economic
Research
Service

Agriculture
Information
Bulletin
Number 499

Farm Sector Financial Problems: Another Perspective

Figure 4

Farm Assets and Equity



Excludes households 1985 preliminary

Falling equity characterizes the farm financial crisis most vividly. Many farmers who borrowed heavily in the late 1970s were not able to cover debt payments from farm earnings alone. Instead, they counted on being able to occasionally borrow against rapidly rising equity values to meet cash flow needs.

Thus, for them, all that was needed to bring on a crisis was for farmland inflation to slow. As we know, land values not only rose more slowly, but actually declined after 1981 (fig. 5).

Farm Debt-to-Asset Ratio Deceptive

Despite rapidly rising debts in the 1970s, the aggregate ratio of debts to assets stayed deceptively stable because asset values also rose rapidly (fig. 6). When asset values began to drop after 1981, the debt/asset ratio soared. Although debts were no longer rising much, asset values were falling.

The farm sector in the 1970s was considered financially solid because its ratio of debts to assets was running well below that typical of other sectors of the economy. That view can be misleading because agriculture uses more capital relative to sales than other sectors of the economy. Most *Fortune 500* corporations, for example, have annual sales in excess of total company assets.

Figure 5

Percent Change in Average Value of Farm Real Estate Per Acre

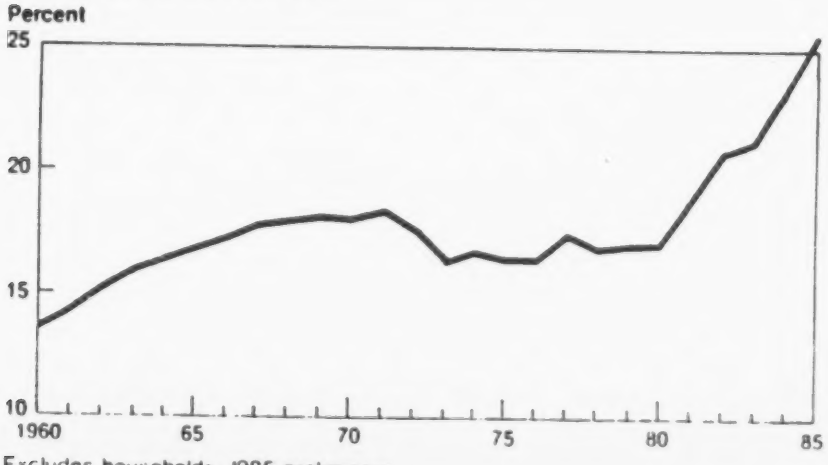


Top No. Change from 1985 to 1986
Bottom No. Change from 1981 to 1986

April 1, 1985 - February 1, 1986 and
February 1, 1981 - February 1, 1986

Figure 6

Farm Debt-to-Asset Ratio



Excludes households. 1985 preliminary.